Pay for home improvements with a cash out refinance

Get the money you need from your home's equity

A cash out refinance can be a great way to use your home's equity to pay for home improvements and repairs. This type of refinancing replaces your current mortgage with a new mortgage with a larger loan amount, and you can use the difference to pay for renovations.

Because the lender gives you a fixed sum of money at one time, cash out refinances are good choices when you want to make major improvements and know how much the work will cost. Consider these pros and cons before you make your decision.

Pros of cash out refinances for home improvements

- You may pay a lower interest rate compared to credit cards or personal loans.
- A fixed interest rate means steady payments for easy budgeting.
- You may be able to get an interest rate on your new mortgage that is lower than the rate on your current mortgage.
- You roll the expenses into your monthly mortgage payment.
- Improvements or renovations may increase your home's value.

Cons of cash out refinances

- You may choose to extend the mortgage term.
- You will likely pay more interest over the life of your new mortgage if you extend the term.
- Depending on market conditions, the interest rate on your new loan could possibly be higher than your existing mortgage.
- You will need to complete a new application, provide income and financial documents, and pay closing costs.

How much money can I get for home improvements?

It depends on how much equity is available in your home. To determine your home equity, determine the fair market value of your house and subtract what you owe on your mortgage. If your house is worth $300,000 and you own $200,000, you have $100,000 in equity.

You can typically tap into a percentage of your home's equity. How much you can borrow is affected by the maximum allowable loan-to-value ratio (or "LTV"), loan type, and other factors. Customers with a VA loan may be able to tap into 100% of their home equity. Here's an example of a customer with a maximum loan-to-value ratio of 80%.

Home value - $300,000
Current mortgage balance - $200,000*
Sample maximum LTV - 0.8 or 80%
Maximum new balance mortgage - $240,000 ($300,000 x 0.8)
Maximum cash available - $40,000 ($240,000 - $200,000)

* If you have additional loans on your home, you need to subtract these from your home value, too.

Remember, some loans have a maximum LTV of less than 80% and closing costs can reduce the amount of cash you get.

Make a plan and budget first

Because cash out refinances require a new mortgage and provide a fixed amount of money, it is a good idea to plan your home improvements and get reliable cost estimates before you apply for the loan. Decide what you want to do and how much you can afford. Also consider material costs, and contractor fees. Research prices, look for professionals with good reputations, and get several bids in writing.

Other ways to pay for improvements

A cash out refinance is not the only way to get money from your home equity. There are also home equity lines of credit (or “HELOCs”), which work like credit cards. HELOCs can be good choices when you don’t know how much money you will need or when you will need it. You can also consider a home equity loan (sometimes called a “second mortgage”). Read our article on these home equity loan choices.

Before using a personal loan or credit card to pay for improvements and renovations, remember they usually charge higher interest rates and have terms that you’ll want to understand before using this type of credit.

Learn more about cash out refinances from Freedom Mortgage

To speak to an experienced loan advisor about cash out refinances, call us at 877-220-5533 or Get Started Today!